

15 August 2016

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submitted via email to comments@pcaobus.org

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**PCAOB Release No. 2016-003, PCAOB Rulemaking Docket Matter No. 034
Proposed Auditing Standard – The Auditor’s Report on an Audit of
Financial Statements when the Auditor expresses an Unqualified Opinion
and Related Amendments to PCAOB Standards**

Dear Sirs,

The IDW appreciates the opportunity to comment on the above mentioned Release, hereinafter referred to as “the Release”.

The IDW also commented on the related Concept Release issued in 2011 and the draft standard proposed in 2013. We continue to support this initiative and refer to our two previous letters in this regard.

In this letter we include comments of a general nature before addressing specific issues or specific aspects of the proposals. We have not responded specifically to the 44 questions posed throughout the Release. However, certain of our comments may be directly relevant to one or more of these questions.

General matters

Support for maximum alignment with the international standards

As the Board will be aware, new audit policy legislation came into force throughout the European Union in June 2016. Amongst other things, this legislation will require enhanced auditor reporting for entities defined as Public Interest Entities (PIEs). The IAASB finalized the revision of its auditor reporting standards in January 2015, with the revised standards effective for audits of

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financial statements for periods ending on or after December 15, 2016. On the global stage, the PCAOB's proposal thus represents a third major initiative in this area.

The IDW is currently in the process of revising the equivalent IDW Auditing Standards so as to transpose the revised auditor reporting ISAs for application within the German legal environment. The first "new style" auditor's report has recently been issued in Germany on the basis of ISA 701.

In previous letters to the PCAOB, the IDW has consistently urged the Board to align its auditing standards to those issued by the IAASB to the maximum extent possible. Consequently, we are pleased to note the Board's acknowledgement that several commenters have urged the Board to work together with other regulators and standard setters to improve the auditor's report. As discussed below, we note significant improvement in this regard, and continue to believe that maximum possible global consistency in auditor reporting is highly desirable.

The IDW appreciates the current proposed standard is a significant improvement in comparison to the 2013 proposal. In particular, the Board has achieved far closer alignment of critical audit matters (CAM) with the IAASB's concept of key audit matters (KAM) than was previously the case. However, elsewhere in this letter, we express our concerns as to an apparent lack of conviction by the Board as to the importance of ensuring that auditor reporting, and reporting of CAM/KAM in particular, will be comparable internationally.

We trust that the Board will give careful consideration to our comments concerning the need for international comparability, and that in pursuing its stated intention to continue monitoring developments of expanded auditor reporting in other jurisdictions throughout the rulemaking process (page 11 of the Release) will seek to achieve maximum comparability going forward.

Implied potential for differences in the matters reported

Enhancing the "pass/fail" auditor reporting model by having auditors report on certain matters arising from an individual audit is the most significant change in auditor reporting in decades. The auditor's report is the main output of an audit that is available to external stakeholders, including investors. In the global environment of today it is increasingly in the interests of both the investor community and the audit profession for there to be as few differences as possible between the content of auditor's reports when different auditing standards are applicable. Consequently, in order to achieve maximum

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comparability standard setters need to consciously limit differences in auditor reporting requirements to those differences that result from jurisdictional particulars. In our view, this is especially important in respect of this “new” area.

The IDW’s main concern relates to the PCAOB’s implied stance in regard to the potential for there to be differences in the matters reported as CAM and KAM, respectively. Firstly, the paper “A Comparison between the ISAs and the US PCAOB Reproposal” prepared by the IAASB’s Auditor Reporting Implementation Working Group points out many similarities, but also refers to the PCAOB’s view that the processes for identifying these matters *would* vary across jurisdictions, and further that the commonalities in the underlying criteria *could* result in the communication of many of the same matters (see pages 10 and 11 of the Release). We believe it extremely unfortunate that this statement equally implies that the Board accepts that its proposals may result in the communication of different matters than would be reported under the ISAs. Secondly, as we discuss below in this letter, in ISA 701.15, the IAASB has determined specific matters that by nature would be KAM, but shall be reported upon differently from other KAMs, whereas the PCAOB proposes a different treatment in terms of their classification and placement of reporting.

We appreciate the Board’s recognition of the potential for differences between the regulatory environment in the United States and other jurisdictions (page 8 of the Release). However, we have not identified discussions within the Release to justify any difference in regard to the nature or number of matters to be reported under CAM and KAM respectively.

In our view, the desire for comparability in terms of matters to be reported is a serious issue that deserves further consideration by all concerned.

Support for not reproposing a standard on “other information”

The IDW agrees with the Board’s decision not to repropose a standard on “other information” at this point in time.

We refer to the response to question 6 in the appendix to the IDW’s letter dated December 11, 2013 in this regard, which detailed certain concerns, including the following:

“However, we believe that actually expanding the responsibility of the auditor to additional procedures or other form of evaluation is not just an auditor reporting matter and therefore requires deliberation in a project that is entirely separate from a project on auditor reporting.” and “Furthermore, we believe that this is a matter that needs

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consideration at statutory (i.e., Congressional) level, if not at least at SEC level that should not be dealt with by auditing standards setting alone.”

We appreciate that these concerns remain to be addressed in a future PCAOB project.

Specific issues

Scope of matters that may be reported by the auditor (Question 7)

We agree that the definition of CAM as well as the detail to be reported concerning CAM should not extend beyond matters in the financial statements. Any reference by the auditor to relevant disclosures outside the financial statements is likely to cause confusion, outweighing any potential benefit. Readers of the auditor’s report would likely assume that a disclosure mentioned by the auditor had also been subject to audit procedures when, in fact, it may not have been subject to audit.

Ability to communicate no critical audit matters (Question 8)

We agree that, whilst probably rare, auditors may encounter audit circumstances in which they determine that no matters meet the definition of critical audit matter.

We also agree that in such cases it is appropriate for the auditor to report this fact.

Clarification of auditor independence (Question 13)

We agree with the proposals relating to the proposed title of the auditor’s report as well as the proposed auditor’s statement on auditor independence.

In our opinion the proposed statement is sufficiently succinct as to clarify to readers of the auditor’s report which independence requirements were applicable to the audit.

Basic elements of the auditor’s report (Question 20)

We note the discussions on page 53 of the Release concerning whether the disclosure of materiality and its application in the audit should be included in the auditor’s report.

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As the following excerpt illustrates, the IDW expressed strong disagreement in its letter to the IAASB (November 29, 2013) when this issue was discussed during that Board's auditor reporting project:

"We ... strongly disagree with the inclusion of the example in paragraph A8 referring to "the application of materiality in the context of the audit". This would encourage auditors to consider the inclusion of a treatment of materiality in the auditor's report, and may in fact encourage the disclosure of quantitative materiality levels. Although we are aware that one jurisdiction has required this, we believe this to be ill-conceived because it ignores the qualitative aspects of materiality – both in terms of ISA 320 and especially in relation to ISA 450 – which cannot be described in any meaningful way in a short-form audit report."

We continue not to support this inclusion, for the reasons explained above.

Other amendments to PCAOB standards (Question 26)

The PCAOB proposals differ from those of the IAASB in one further key respect.

In ISA 701.15, the IAASB determined that 1) a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern or 2) a matter giving rise to a qualified opinion or 3) an adverse opinion, would by their nature constitute key audit matters. However, ISA 701.15 also prescribes that these matters shall not be reported as KAM. The section on KAM shall instead include a reference to the appropriate section in the auditor's report that deals with the matter (i.e., sections entitled, or "Material uncertainty related to going concern", "Basis for qualified opinion" or "Basis for adverse opinion").

In contrast, when the auditor expresses a qualified opinion proposed AS 3105.02, would require the same communication of CAM as would be required in an unqualified auditor's report under AS 3101. The note following AS 3105.04 directs the auditor to refer to AS 3101 to determine if the matter for which the auditor qualified his or her opinion is also a critical audit matter. These requirements are in addition to the requirement for the auditor to disclose the substantive reasons for the qualified opinion.

In respect of adverse opinions, the PCAOB proposals stipulate that the requirements as to CAM do not apply (see Note following AS 3105.40). Thus there is no equivalent to the reference within the KAM section of the auditor's report as required under ISAs.

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We are concerned that these differences in placement of information and potential differences in classification impact comparability of auditor's reports, and may be particularly confusing for those readers who will read auditor's reports prepared under the ISAs and the PCAOB standards, especially where statistics e.g., on number of (CAM/ KAM) matters reported are collated.

If you have any questions relating to our comments in this letter, we should be pleased to discuss matters further with you.

Yours truly,

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Executive Director

Gillian Waldbauer
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